

**Memorandum of Decision: 01-20200164R
Individual Income Tax
For the Year 2017**

NOTICE: IC § 4-22-7-7 permits the publication of this document in the Indiana Register. The publication of this document provides the general public with information about the Indiana Department of Revenue's official position concerning a specific set of facts and issues. The "Holding" section of this document is provided for the convenience of the reader and is not part of the analysis contained in this Memorandum of Decision.

HOLDING

Individual provided information to show that his original return was correct as reported, however Individual failed to provide evidence that his protest was timely.

ISSUE

I. Income Tax - Imposition.

Authority: IC § 6-8.1-5-1; IC § 6-8.1-8-2; IC § 6-8.1-8-4; IC § 6-8.1-10-2.1; IC § 6-8.1-10-1; [45 IAC 15-3-2](#); 26 U.S.C. §§ 671, 678.

Taxpayer protests Department's denial of its refund claims.

STATEMENT OF FACTS

Taxpayer is a non-resident who has ownership interests in various Indiana entities. Some of his ownership interests are direct and some are through a family trust. Taxpayer receives income from these entities and the entities remit withholding tax based on that income. Taxpayer filed his 2017 Indiana return in a timely manner. On that return Taxpayer reported the income and withholdings which flowed through to him from the Indiana entities. The Indiana Department of Revenue ("Department") disallowed the reported withholdings resulting in an assessment that was eventually garnished from Taxpayer's bank account. Taxpayer contacted the Department's Taxpayer Advocacy Office ("TAO") which determined that the garnishment was made in error, and refunded Taxpayer an amount equal to base tax but did not refund the originally claimed refund, collection fees, or penalties.

The Department performed a second review of Taxpayer's 2017 return. In that review, the Department was able to verify Taxpayer's withholdings, however, the Department determined that Taxpayer's Indiana income was underreported. The result was a much smaller refund than Taxpayer claimed on his original return. Taxpayer claims that this was the result of a disallowed loss carry forward and he is entitled to a refund equal to his originally claimed refund plus collection fees and penalties.

Taxpayer protested and an administrative hearing was held. This decision is based on the information provided with the protest, in the hearing, and in the Department's records. Additional facts will be provided as necessary.

I. Income Tax - Imposition.

DISCUSSION

Taxpayer is a non-resident individual who has ownership in several Indiana entities both directly and through a family trust. Taxpayer timely filed his 2017 Indiana return on which he claimed a refund. The Department denied the refund and issued a proposed assessment. After proceeding through the normal stages of proposed assessment and then demand notice, the assessment eventually staged to warrant and was garnished from Taxpayer's bank account. Taxpayer contacted TAO and it was determined that the garnishment was made in error. The Department refunded Taxpayer the base tax portion of the assessment but did not refund the originally claimed refund, collection fees, or penalties. Further, the Department performed a second review of Taxpayer's 2017 return in which it verified the reported withholdings but increased the reported income substantially. The result was a much smaller refund than originally reported.

A. Collection Fees

Taxpayer argues that because his original return was filed timely and reported correctly, he is entitled to a refund of collection fees charged to him as a part of the garnishment.

If the Department reasonably believes that a taxpayer has not reported the proper amount of tax due, the Department shall propose an assessment of unpaid tax based on the best information available to the Department. IC § 6-8.1-5-1(b). The amount of the proposed assessment "is considered a tax payment not made by the due date" and is subject to penalties and interest. *Id.* Notice of the proposed assessment shall be sent to the taxpayer stating that it has sixty (60) days in which to pay the assessment or file a written protest. IC § 6-8.1-5-1(b) and (d). If the taxpayer does not pay the proposed assessment or file a written protest in the sixty (60) day period "[t]he department shall demand payment, as provided in IC § 6-8.1-8-2(a), of any part of the proposed tax assessment, interest, and penalties . . ." IC § 6-8.1-5-1(j).

IC § 6-8.1-8-2 provides that the Department must issue a demand notice for payment which grants the taxpayer ten days in which to "either pay the amount demanded or show reasonable cause for not paying the amount demanded." IC § 6-8.1-8-2(a). If a taxpayer "does not pay the amount demanded or show reasonable cause for not paying the amount demanded within the twenty (20) day period, the department may issue a tax warrant for the amount of the tax, interest, penalties, collection fee, sheriff's costs, clerk's costs," and other fees. IC § 6-8.1-8-2(b). When it has issued a tax warrant, the Department may contract with a collection agency to collect delinquent tax plus interest, penalties, collection fees, and other fees and costs. IC § 6-8.1-8-4(a). Additionally, "a collection fee of ten percent (10 percent) of the unpaid tax is added to the total amount due." IC § 6-8.1-8-2(b). When a tax warrant is filed, "the total amount of the tax warrant becomes a judgment against the person owing the tax." IC § 6-8.1-8-2(e).

Taxpayer's proposed assessment notice was issued on December 7, 2018. The assessment instructed Taxpayer to "pay the amount owed or protest this tax assessment in writing within 60 days (by February 5, 2019). If you fail to do so, this tax debt will continue to accrue interest and could convert into a tax warrant for collection action." According to Taxpayer's representative, she contacted the Department upon receipt of the notice and was informed that the trust returns and K-1s needed to be filed. During the hearing, Taxpayer provided a protest letter, dated January 25, 2019, which Taxpayer claims to have mailed to the Department. The letter was addressed to the address provided on the tax assessment and included copies of grantor letters from the family trusts, trust returns and related K-1s. It is unclear whether the Department received that information, though Department records do not reflect receipt of that letter and Taxpayer was unable to provide any proof of mailing.

Because the Department did not receive the January 25th protest letter the assessment progressed to a demand notice which was issued on April 15, 2019. That notice instructed Taxpayer to "pay the amount owed no later than May 6, 2019 or show reasonable cause with supporting documentation for not paying. Failure to do so will convert this notice to a tax warrant and be referred for immediate collection action. . . ." Again, Taxpayer's representative states that she called the Department and spoke with a Department employee. Taxpayer's representative relayed that she was told that the Department was processing the trust returns and a hold would be placed on Taxpayer's account. No record of this conversation exists in the Department's records. Further [45 IAC 15-3-2\(e\)](#) provides that "[o]ral opinions or advice will not be binding upon the department." Thus, the Department cannot be bound by whatever information was relayed in this conversation. The assessment staged to warrant and was turned over to the Department's third-party collection agency. That agency issued a notice to Taxpayer on June 28, 2019 which included instructions for payment. That notice was again issued on July 1, 2019. Taxpayer's bank account was garnished on July 5, 2019. The garnishment included tax, collection fees, and penalties.

After garnishment, Taxpayer contacted TAO and submitted all requested information. Based on that information, TAO determined that the garnishment was made in error, and refunded the tax, but not the collection fees or penalties. Collection fees are a statutorily allowed amount for collection on a tax warrant, even if the liability is later revised. According to Department records, Taxpayer did not pay or protest the assessment. Taxpayer did not provide proof that its January 25, 2019 letter was mailed to or received by the Department. Collection fees are not retained by the Department and in the absence of Department error, the Department is not able to refund those fees. Taxpayer failed to demonstrate that the Department acted improperly at any stage of the collections process or that the Department was somehow at fault. Therefore, Taxpayer's protest of collection fees is denied.

B. Original Refund Claim

As stated above, Taxpayer receives income from ownership in Indiana entities both directly and through family trusts. The family trusts are grantor trusts and Taxpayer is the grantor. According to 26 U.S.C. §§ 671, 678, the grantor is treated as owner of the trust and must include, in computing his individual taxable income, the income,

deductions, and credits generated by trust property. As such, Taxpayer included those items in his 2017 return. Additionally, Taxpayer had withholding on some of his Indiana income, which he also reported on his return.

In 2016, one of the family trusts incurred a large loss, a portion of which Taxpayer reported on his 2016 return. Substantially all of that loss was carried forward to 2017 and included in Taxpayer's Indiana income. The Department reviewed Taxpayer's 2016 income tax return, K-1s and Basis Schedule. The loss was included in Taxpayer's income calculation on Statement 2 to Schedule A. The loss was also calculated in Taxpayer's Basis Schedule. Based on this review, the loss carry forward was appropriate and the Indiana income as reported was appropriate. The Department will adjust its records to reflect that loss.

Because the Department verified both Taxpayer's 2017 Indiana withholdings as well as his Indiana income, Taxpayer is sustained and entitled to his originally claimed refund.

C. Penalty and Interest

The remaining issue is whether Taxpayer is entitled to a refund of penalty and interest imposed on the assessment. When the Department was unable to verify Taxpayer's reported withholdings, it issued a proposed assessment. According to IC § 6-8.1-5-1(b), "[t]he amount of the assessment is considered a tax payment not made by the due date and is subject to IC [§] 6-8.1-10 concerning the imposition of penalties and interest."

The penalties imposed on Taxpayer's proposed assessment were done under the authority of and requirements set forth in IC § 6-8.1-10-2.1(a) which, for the tax year at issue, provides as follows:

Except as provided in [IC 6-3-4-12\(k\)](#) and [IC 6-3-4-13\(l\)](#), a person that: (1) fails to file a return for any of the listed taxes; (2) fails to pay the full amount of tax shown on the person's return on or before the due date for the return or payment; (3) incurs, upon examination by the department, a deficiency that is due to negligence; (4) fails to timely remit any tax held in trust for the state; or; (5) is required to make a payment by electronic funds transfer (as defined in [IC 4-8.1-2-7](#)), overnight courier, or personal delivery and the payment is not received by the department by the due date in funds acceptable to the department; is subject to a penalty.

However, "[i]f a person subject to the penalty imposed under this section can show that the failure to file a return, pay the full amount of tax shown on the person's return, timely remit tax held in trust, or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall waive the penalty." IC § 6-8.1-10-2.1(d).

The Department does not believe that the Taxpayer was acting negligently in this instance. Once Taxpayer provided the requisite trust returns and K-1s the Department was able to verify the reported withholdings and determine the garnishment was in error. Therefore, Taxpayer's protest, as it pertains to penalties, is sustained.

With respect to the interest imposed on Taxpayer's assessment, Indiana imposes interest on overdue tax pursuant to IC § 6-8.1-10-1(a), which states:

If a person fails to file a return for any of the listed taxes, fails to pay the full amount of tax shown on the person's return by the due date for the return or the payment, or incurs a deficiency upon a determination by the department, the person is subject to interest on the nonpayment.

IC § 6-8.1-10-1(e) further provides that the Department may not waive interest. Therefore, to the extent that interest remains, the Department is statutorily prohibited from waiving any such interest.

FINDING

Taxpayer is sustained in regard to its original refund claim and penalties; however, Taxpayer's protest of collection fees and interest is denied.

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